

## **ARTICLE FOR *SQUARE FEET* – January 15, 2008**

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### **COMMERCIAL LEASES – STRATEGIES WHEN THE STORM CLOUDS OF A SOFTENING ECONOMY LOOM**

The general destabilization of the national economy in recent months, while having a somewhat reduced impact on Oklahoma, is still being felt by the state's real estate industry in a variety of ways. This column will focus on one aspect of this industry, existing commercial Landlord-Tenant relationships, and explore what happens when economic forces pressure those relationships to the point where something has to give.

We have all seen the signs before - monthly rent checks begin arriving late, inventory is down, the parking lot is rarely full, etc. And all too often, the iceberg principal is at work. What you see of the economic troubles is but a small part of what is really happening. At some point, and the sooner the better is certainly true, the Tenant has to come to grips with the current and future financial realities of its operations.

#### **TIPS FOR THE TENANT**

Regardless of how tough the financial situation may be, if a Tenant is going to approach its Landlord about economic assistance or concessions, there are a few key things to keep in mind:

- Get your act together. Assemble all the financial information you can on your overall operations and put it in an understandable form. Reply to Landlord requests for additional information promptly and completely.
- Have a plan, and not just one for how to get through the next month or two. A Landlord (who by the way is probably experiencing its own financial stresses) needs to be convinced that you have thought your situation through thoroughly and reached some meaningful and relatively accurate conclusions as to your economic future.
- Be realistic. Nothing becomes obvious more quickly than when your strategy for long term survival is based on a hope and a prayer. Landlords just stop listening at that point and you can't blame them.
- Put all your cards on the table – and make sure they are all face up. Nothing undermines what might otherwise be, at least initially, positive discussions on possible economic concessions by a Landlord than finding out that the Tenant has

been less than completely open about all matters that impact its operations and future.

- Be willing to appreciate the Landlord's position and entertain reasonable compromise proposals. Remember, in all likelihood the silent but nonetheless significant player at the negotiating table is the Landlord's Lender.
- Don't expect something for nothing. You will have to make meaningful concessions (e.g. higher future rent if your looking for short term rent reductions, additional collateral or Lease guaranties, etc.), and not ask the Landlord to absorb the major brunt of your current financial situation.

### **TIPS FOR THE LANDLORD**

While Landlords are perhaps in a better legal position where they are dealing with an already or soon to be defaulting Tenant, as often happens, things are seldom as simple as they might first appear. Particularly in a soft (or worse) economy, the loss of every Tenant has a material impact on a Landlord's or project's continued viability. So some suggestions for Landlords:

- Be wary but open. At least initially a Landlord can expect to receive the picture and plan most beneficial to the Tenant, but as a dialogue ensues particularly coupled with improving Tenant credibility and a more balanced view of the Tenant's actual situation, unanticipated opportunities and strategies can present themselves, which can be missed if the Landlord is not careful.
- Resist the temptation to horse-trade. You expect frankness and transparency from your economically stressed Tenant, so be willing to offer some of the same back across the table.
- Don't fight battles that aren't worth winning. You can threaten and even pursue contractual and legal remedies (and frankly you should if your Tenant has under disclosed or worse, misrepresented its situation), but given the costs of litigation and the uncertainty in actually collecting on debts and judgments in troubled economic times (not to mention the specter of a possible Tenant bankruptcy), a "win" for the Landlord in the technical sense can and often does result in a net loss overall.
- Be tough but pragmatic. You know, and your Tenant at least suspects, that if it cannot make a go of it under the current Lease terms and Landlord refuses to compromise in meaningful ways, Tenant will be gone and you will find replacement Tenant prospects to be marginal given the distressed economy.
- Critically analyze the Tenant's plan and proposal, even if that means that you end up concluding that there is no reasonable prospect of the Tenant's long term survival. While as they say, hope springs eternal, sometimes it is better to acknowledge that it's over when it really is.

Overall, when a Tenant approaches a Landlord about the possibility of restructuring at least for the near term, the economic elements of an existing Lease relationship, perhaps the best advice both parties can benefit from is to be willing to listen, a lost art in markets such as we have experienced for the last several years when everybody seemed to make money almost regardless of how they operated. But times like these require a different and more flexible mindset to cope with and even succeed during, a slowly eroding economic base.